

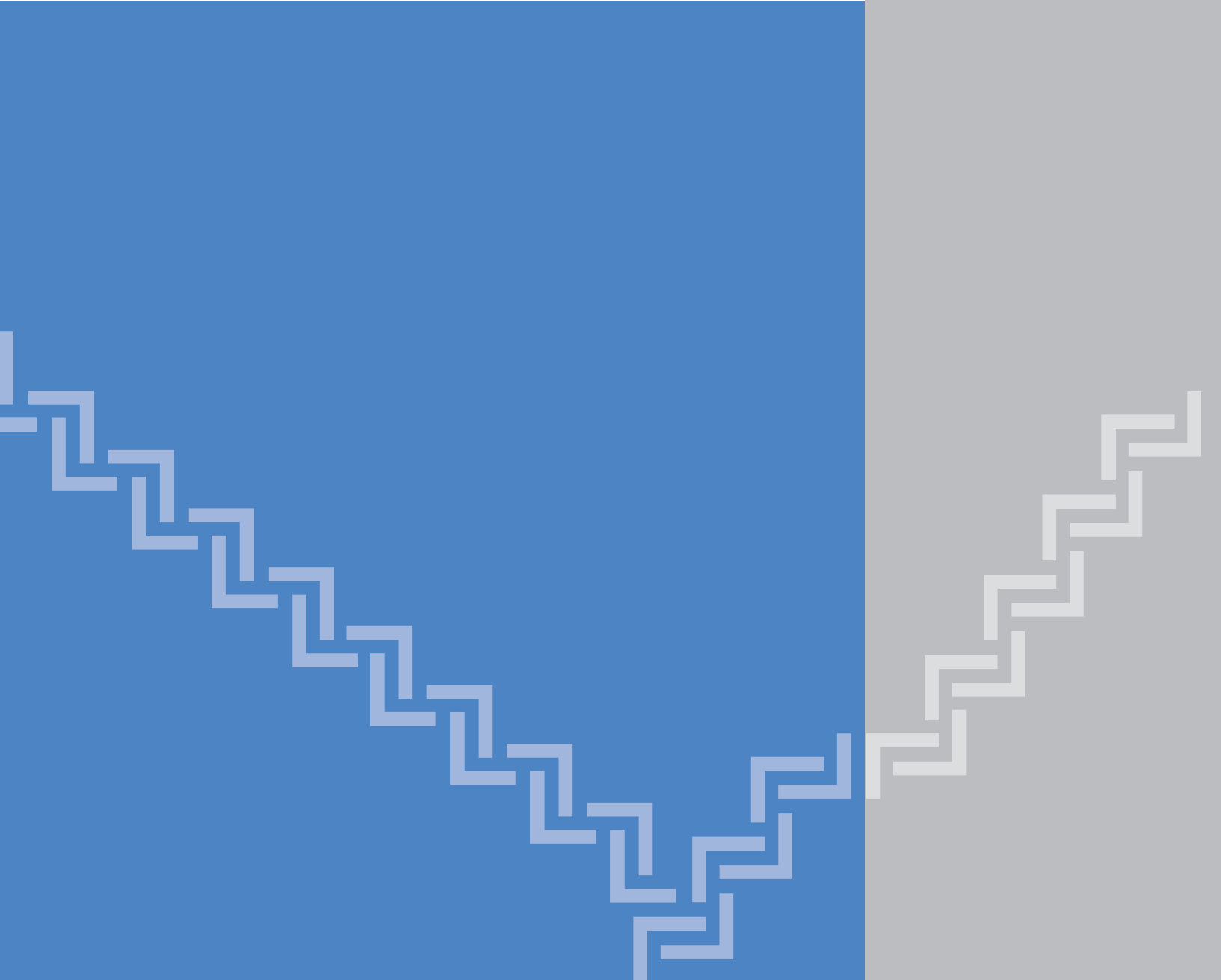


THE MONEY MANAGEMENT INSTITUTE



The State of Model Portfolio Programs

MMI REPORT
2007



Dover Financial Research, LLC is a boutique research and consulting firm, specializing in the financial services industry. For more information about the firm, please visit www.doverfr.com or call 781.461.0922.

The Money Management Institute (MMI) is the national organization for the managed accounts solutions industry, representing asset management firms, program sponsors and service providers. More information is available by visiting www.moneyinstitute.com or calling 202.822.4949.

© 2007 The Money Management Institute – All Rights Reserved. *No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photography, recording, or any information storage or data retrieval system, without written permission from The Money Management Institute. MMI will regularly grant this permission to members upon request.*

TABLE OF CONTENTS

INDEX OF EXHIBITS 2

METHODOLOGY 4

PREFACE 5

INTRODUCTION 6

Benefits of Model Portfolio Programs 6 • Definition of Overlay Portfolio Management 7

FRAMEWORK OF MODEL PORTFOLIO PROGRAMS 8

Position in Advisory Market 8 • Four Approaches to Delivering the Manager's Model 8

MARKET LANDSCAPE FOR MODEL PORTFOLIO PROGRAMS 11

Managed Account Solutions Industry – Growth Continues

Market Size – Model Portfolio Programs • Distribution Channel Statistics

Asset Manager Participation • Program Composition – Key Attributes

OVERLAY PORTFOLIO MANAGEMENT

Asset Manager and Sponsor Firm Perspectives • And the Answer Is – Quantitative Findings

MAJOR CHALLENGES TO GROWTH

Manager and Sponsor Reluctance • Trading Complexities

Fixed Income and Alternative Investments • Performance Reporting and Dispersion

Client and Advisor Adoption • Advisor Support

ECONOMICS – THE BIGGEST CHALLENGE TO MODEL PORTFOLIO PROGRAMS

Emerging Economics • Investment Management - Fee Compression

Economic Implications for Asset Managers

INDUSTRY OUTLOOK

Model Portfolio Programs – Growth Projections

The Traditional SMA Market – Future Prospects

INDEX OF EXHIBITS

1. Benefits of Unified Managed Account Programs **6**
2. SMA Evolution: From Single Product Programs to Multi-Product Platforms **8**
3. Four Approaches to Delivering the Manager's Intellectual Capital **9**
4. MAS Assets by Market Segments (\$ billions)
5. MAS Industry – Hierarchy of Major Market Segments (\$ billions), 2Q 07
6. Breakdown of SMA Market (\$ billions), 2Q 07
7. Growth in UMA Assets (\$ billions), 2005-2Q 07
8. % of UMA/MDP Assets by Type of Model Delivery, 2Q 07
9. UMA/MDP AUM by Type of Model Delivery (\$ billions), 2Q 07
10. SMA Market by Major Segment and Model Delivery Type, Assets and Market Share (\$ billions), 2Q 07
11. % of Model Portfolio Programs Affiliated with Legacy v. Emerging Platforms, 2Q 07
12. % of UMA Assets, Wirehouse v. Non-Wirehouse, 2005 v. 2Q 07
13. Model Portfolio Programs – % of AUM by Channel and % of Total Programs by Channel, 2Q 07
14. Wirehouse v. Non-Wirehouse UMA/MDP Assets by Model Delivery Type, 2Q 07
15. Growth in the Number of Managers Providing Models, 2Q 07
16. Breakdown of Asset Managers Participating in Model Portfolio Programs by AUM, 2Q 07
17. Breakdown of Participating Manager Assets: Mutual Fund v. SMA, 2Q 07
18. Top 10 SMA Managers Participating in Model Portfolio Programs, 2Q 07
19. Strategies Participating in Model Portfolio Programs, 2Q 07
20. Number of Strategies Offered per Manager, 2Q 07
21. Number of Model Portfolio Programs by Manager, 2Q 07
22. Percentage of Discretionary v. Nondiscretionary Programs, 2005 to 2Q 07
23. Model Portfolio Program Asset Allocation Approach, 2Q 07
24. Model Portfolio Programs – Manager Selection Approach, 2Q 07
25. Product Composition of Model Portfolio Programs, 2Q 07
26. Product Composition, % of Assets by Product Type, 2Q 07
27. Average Account Size, 2Q 07
28. Sponsors Perspective on Overlay Management, 2Q 07
29. SMA Managers' Perspectives on Overlay Management, 2Q 07

30. Overlay Portfolio Management Capabilities Most Valued by Sponsors, 2Q 07
31. Overlay Portfolio Management Capabilities Least Valued by Sponsors, 2Q 07
32. Overlay Portfolio Management Capabilities Most Valued by Asset Managers, 2Q 07
33. Overlay Portfolio Management Capabilities Least Valued by Asset Managers, 2Q 07
34. Utilization of Tax Management Tools, 2Q 07
35. % of Taxable Accounts Using Tax Management Capabilities by Program, 2Q 07
36. Breakdown of Overlay Capabilities % Utilization Per Program, 2Q 07
37. Utilization of Client Customization Capabilities, 2Q 07
38. Overlay Providers by Firm Type – Outlook, 2Q 07
39. Obstacles to Model-Based Delivery as Ranked by Program Sponsors, 2Q 07
40. Obstacles to Model-Based Delivery as Ranked by Asset Managers, 2Q 07
41. Type of Manager Participating in Model Portfolio Programs, 2Q 07
42. % of Asset Managers Participating in Model Platforms, 2Q 07
43. Asset Manager Participation by Investment Discipline, 2Q 07
44. Challenges to Advisor Adoption, Sponsor Perspective, 2Q 07
45. Estimated SMA All-In Client Fee (Actual) in Basis Points, 1998–2006
46. Basic Overlay Portfolio Management Fees, 2Q 07
47. Overlay Portfolio Management Fees, Basic Overlay Compared to Robust Overlay, 2Q 07
48. Hypothetical Comparison of Platform Economics in Basis Points, 2Q 07
49. Range in Investment Management Fees in Model Portfolio Programs, Large Cap Equity SMA Strategies, 2Q 07
50. Range in Investment Management Fees by Model-Based Delivery Type, Large Cap Equity Strategies, 2Q 07
51. Financial Risk to Asset Managers Associated with Shift to Model Portfolio Programs
52. % of Firms and Assets by Pricing Strategies
53. Managed Account Solutions Market Segments Representing the Greatest Opportunity for Growth, 2Q 07
54. Sponsors' Vision for Advisory Platforms, 2Q 07
55. % of Retail Separate Accounts Shifting to Model Portfolio Programs, 3-year Projection, 2Q 07
56. % of Retail Separate Accounts Shifting to Model Portfolio Programs, 5-year Projection, 2Q 07
57. Shift in Assets from Traditional SMA Programs to Model Portfolio Programs

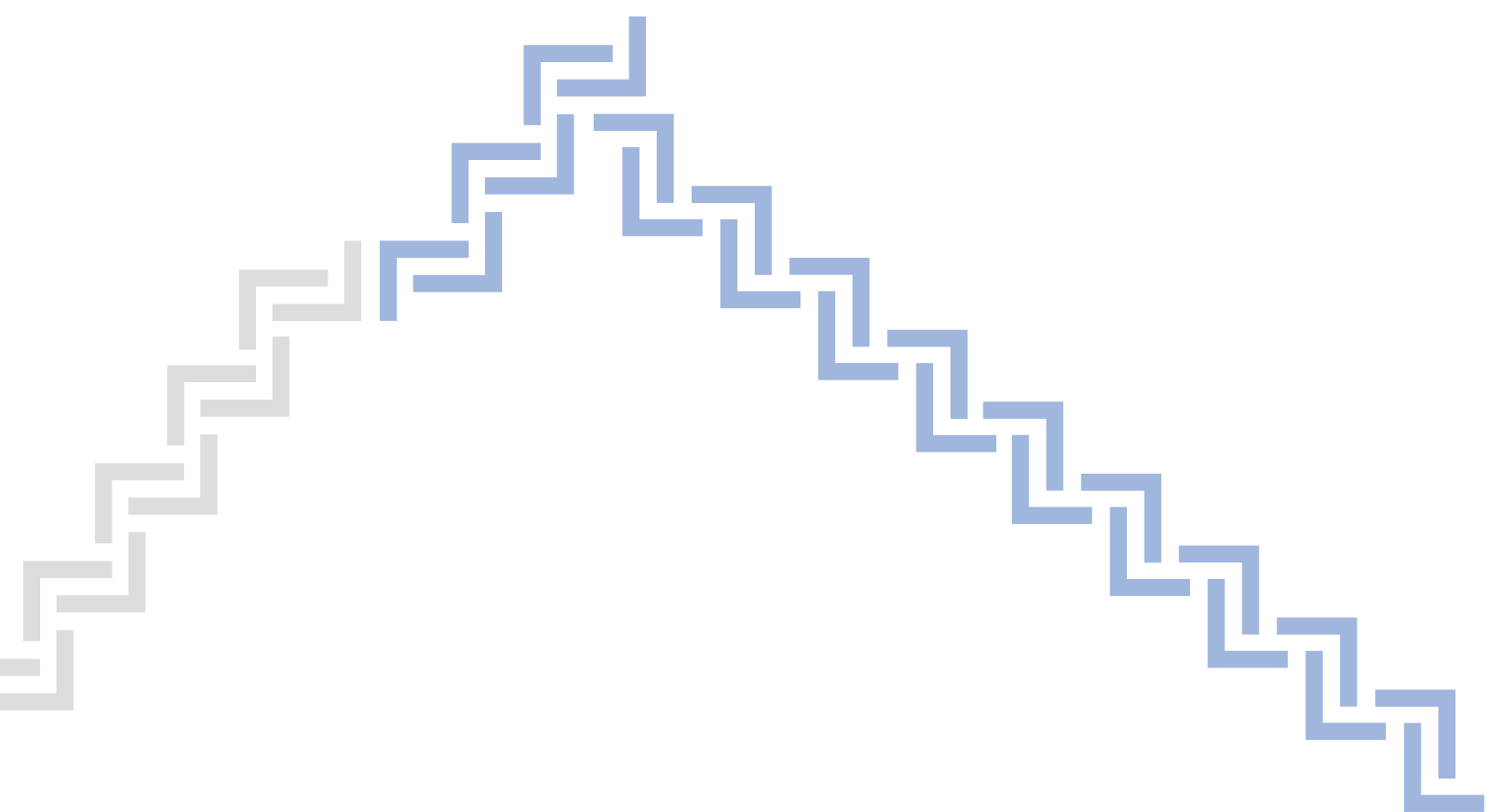
METHODOLOGY

The following research focuses on *model portfolio programs* within the brokerage industry. The data and analysis contained herein was compiled from numerous rounds of in-depth interviews and multiple quantitative surveys.

Qualitative analysis was derived from more than 60 interviews with executives representing the following types of firms: wirehouses, regional and independent brokerages, banks, overlay portfolio managers, service providers and asset management firms.

In addition, three quantitative surveys were conducted yielding the quantitative analysis found in this report. Data from these surveys have been compiled into a proprietary research database and represent the most comprehensive repository of information related to model portfolio programs.

Finally, MMI, in conjunction with Dover Financial Research, continues to lead the market in identifying and examining emerging trends that significantly influence the managed account solutions industry.



PREFACE

Dover Financial Research, LLC was engaged by MMI to conduct proprietary research into the development and proliferation of model portfolio programs. The goal of this research is to provide an overview of the industry, to analyze the benefits and challenges associated with these programs, and to provide a prognosis of the direction in which the industry is heading.

For purposes of definition, *model portfolio programs* include any advisory program in which an underlying SMA manager provides its investment model (or models) to an overlay manager. Model-based delivery is another term used interchangeably with model portfolio programs to describe the way these programs operate. A hypothetical example would be an investment manager such as Neuberger Berman passing its investment model to an overlay manager such as Placemark or Parametric, or even Merrill Lynch.

Our research indicates that model portfolio programs benefit investors by providing an efficient way of delivering comprehensive, customized financial solutions in the form of a single account. Looking ahead, we believe these programs will be used to provide financial solutions to a wide swath of clients—ranging from mass affluent to high net worth individuals. In addition, sponsor firms that are able to perfect the development of these platforms by integrating alternative products, providing access to best-of-breed managers, unbundling pricing, and, above all, making it easy for the financial advisor to create customized portfolios will have a competitive advantage in the marketplace. As a result, model portfolio programs represent the next significant phase in the evolution of advisory programs.

Not all model portfolio programs are alike, however. They vary in terms of how they operate, from pure model-driven programs to those that provide flexibility with regard to trading and pricing. The overlay element of the program can play either a large or supporting role.

In any event, the transition to model portfolio programs will not happen over night. The obstacles standing in the way of widespread adoption of these programs—including the inability to seamlessly integrate pure alternative products, trading rotation issues, manager participation and advisor adoption—are substantial.

In the short term, these obstacles will thwart the growth of model portfolio programs. But as the industry overcomes the challenges and better comes to grips with the risks, model portfolio programs will represent a compelling solution for the financial advisor and will eclipse other types of product-specific programs, such as mutual fund wrap and SMA wrap. Therefore, we believe the future of these programs is bright.